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Taxation -- Receipts of Non-Profit Club from Its Members Held Not Exempt Under Section 101(9) of Internal Revenue Code

to realty. To allow courts to liberally interpret statutes which are in derogation of the common law will undoubtedly increase the confusion with the concomitant perplexity as to the ownership of realty. However, the decision of the court in the instant case will be followed, purportedly because of the incapacity of the trustees to contract away public property, but in reality on the basis of public policy.

TAXATION—RECEIPTS OF NON-PROFIT CLUB FROM ITS MEMBERS HELD NOT EXEMPT UNDER SECTION 101(9) OF INTERNAL REVENUE CODE

Petitioner, member club of the American Automobile Association, was a non-profit group organized primarily to furnish services to its members at a lower price than such services could be obtained elsewhere had the members acted individually. Petitioner did not itself furnish labor or material for these services but merely procured them for its members. It issued no shares of stock and paid no dividends. Its charter required that its assets be transferred to another non-profit organization in case of dissolution. The Commissioner sought to collect federal income tax on receipts of petitioner in the form of dues and entrance fees. Petitioner contended that it was exempt from tax under Section 101(9) of the Internal Revenue Code[1] as a non-profit organization. *Held*, that since petitioner was engaged in a business of a kind generally carried on for profit, and since its members received services at a discount from the usual market price, it was not exempt under Section 101(9). *Chattanooga Automobile Club v. Commissioner of Internal Revenue*, 12 T. C. No. 29 (1949).[2]

The holding of the principal case, if affirmed on appeal, will constitute a landmark in the law of federal income taxation. The idea is a novel one indeed that a non-profit organization, formed for the purpose of securing services cheaper for its members, should be subject to federal income tax on the dues and other fees paid by the individual members in order to make possible the availability to them of such services. From earliest days farmers, fruit growers, merchants, and other entrepreneurs have formed associations for the express purpose of buying collectively to effect savings over individual buying costs. The resulting intake of the association or club from its individual members has universally been held tax exempt. In a subsequent section of the Internal Revenue Code[3] farmers' marketing and purchasing cooperatives

1. "The following organizations shall be exempt from taxation under this chapter—. . . (9) Clubs organized and operated exclusively for pleasure, recreation, and other nonprofitable purposes, no part of the net earnings of which inures to the benefit of any private shareholder. . . ."

2. See also the companion case, Keystone Automobile Club v. Commissioner of Internal Revenue, 12 T. C. No. 134 (1949).

3. INT. REV. CODE § 101 (12).

are specifically exempted from federal income tax. Even consumers' cooperatives, which enjoy no such statutory exemption, have been exempted, by administrative practice, as long as their excess of receipts over disbursements is turned back to the co-op members.[4] No "profit" is said to accrue to the cooperative; and this is true even where the excess receipts are not distributed to the members in cash.[5]

Granting that the tax exemption presently afforded to consumers' cooperatives is not warranted in certain situations, a debatable admission at best, certainly clubs organized for non-profitable purposes fall within the tax exempt category as conceived by Congress. Under the language of the governing statute itself, clubs ". . . operated for . . . nonprofitable purposes, no part of the net earnings of which inures to the benefit of any private shareholder . . ." are exempt from the income tax. One could hardly describe the situation of petitioner in the instant case in more adequate phraseology. Admittedly, services were made available to members at a discount from the regular market price. But this was the very reason for petitioner's existence, just as in the case of any collective buying venture. The court confuses "profits" with savings. If *A* buys a watch on Monday at the *X* jewelry store for the price of $10, but *B* purchases the same model watch on Tuesday for $9, the conclusion that *B* has made a *profit* on the transaction would be little short of ludicrous.[6] True, *B* may have *saved* $1, but that dollar is certainly not taxable as a profit under the federal income tax laws.[7] More than that, petitioner had no stockholders in its organization. The gains involved accrued to its members. It simply acted as a *purchasing agent* for those members, not as a corporate distributor of profits to absentee investors. The mere receipt, even by an organization for profit, of money or property has never implied taxable income.[8] Nor have the courts labeled intake as taxable income although distribution of the excess of receipts over disbursements was made to shareholders.[9] The presence of receipts in the treasury of petitioner should have been held a trust fund belonging to its individual members. "Even Congress can't make income out of something which is not income in fact."[10] An appellate court should have little difficulty in finding grounds for reversal of the holding in the instant case.[11]

4. See Sowards, *Should Co-ops Pay Federal Income Taxes?*, 19 TENN. L. REV. 908 (1947).
5. *Id.* at 917.
6. See O'Meara, *The Federal Income Tax in Relation to Consumer Cooperatives*, 36 ILL. L. REV. 60 (1936).
7. See Uniform Printing and Supply Co. v. Comm'r., 88 F.2d 75 (C. C. A. 7th 1937).
8. Farmers' Union Cooperative Co. v. Comm'r., 90 F.2d 488 (C. C. A. 8th 1937).
9. *Ibid.*
10. Burk-Waggoner Oil Ass'n. v. Hopkins, 269 U. S. 110, 114 (1925).
11. California State Automobile Ass'n. v. Smyth, 77 F. Supp. 131 (N. D. Calif. 1948).